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SUBJECT: Austrians Push EU to Help Banks on Eastern  
Frontier

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¶1. SUMMARY: The Austrian government announced January 27 it will press the EU to help the financial sectors in Central, Eastern and Southeastern Europe (CESEE) in the wake of the global credit crisis and global downturn. Last week, the GoA assembled key regional players (including the IMF) for closed-door talks. Spearheaded by Austria's Raiffeisen International (RI), nine large EU banks active in CESEE announced they will lobby for the EU and ECB to work with local governments in assisting banks in the region. Banking risks in CESEE have grown significantly in past weeks because of spillover from Western Europe's deepening recession. With assets of EUR 228 billion in CESEE, Austrian banks are the biggest lenders in the region, followed by German and Italian banks. END SUMMARY.

GoA Pressing Europe to Aid CESEE Banks  
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¶2. On January 23, the GoA hosted a meeting of representatives from the Austrian National Bank (OeNB), the Austrian Financial Market Authority (FMA), the EBRD and the IMF to discuss how to bolster ailing CESEE/CIS economies, support banks active in those countries (including foreign banks), and prevent a downward liquidity spiral in the region. (Austrian officials characterized it as a pre-scheduled meeting and not a "crisis" gathering).

¶3. On January 27, Chancellor Werner Faymann and Finance Minister Josef Proell followed-up the meeting with an announcement that Austria will push for an international stabilization/aid package to help banks and the region's economies to weather the current crisis. PM Faymann and FinMin Proell argued that such aid will help the EU's member states (including Austria) whose banks are heavily exposed in the region. Austria's leadership want the IMF, EU, ECB, EIB and the EU's Cohesion Fund to join in a coordinated package. The GoA initiative also calls on countries such as Bulgaria, Romania and the Ukraine to devise national measures to shore up their banking sectors.

Road Show to Promote the Initiative  
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¶4. Faymann will raise the issue with German Chancellor Angela Merkel during his January 28 visit. Beyond Germany, the GoA is seeking support from France, Italy and Belgium -- the most important investors in CESEE -- and the EU Presidency (Faymann will soon visit Czech

Premier Mirek Topolaneck). Senior Austrian officials, including PM Faymann and FinMin Proell, will also visit key CESEE countries to promote the initiative. Key for Austrian interests (and those of other wealthy EU member states) is that the initiative would also help Western banks doing business in emerging Europe.

#### Rapid Deterioration of the Situation in CESEE

15. The unexpectedly sharp real downturn in Western Europe is spreading to CESEE countries, whose financial situation (especially in countries dependent on exports to/capital imports from Western Europe) has deteriorated faster than expected. Downward revisions to Eurozone forecasts mean that many CESEE/CIS countries, originally projected to grow in much of 2009, are expected now to fall into recession. The IMF recently downgraded its economic prospects for CESEE and warned of credit crises in the region, whose challenges include a sharp dip in exports (exacerbating the large current account deficits of many countries in the region), current account financing problems, the depreciation of local currencies vis-a-vis the dollar and the Euro (causing severe repayment problems for local borrowers who have taken out hard currency loans), and rumors of 1993/1998-style hedge fund speculation against local currencies.

#### Austrian Banks Have a Huge Stake in CESEE/CIS Health

16. With outstanding loans of around EUR 228 billion in

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CESEE/CIS, Austrian banks are the biggest lenders in the region, followed by German and Italian banks. CESEE exchange rate weakness has turned out to be a bigger problem for banks than anticipated, as it calls into question the credit worthiness of many loan assets in the region. Helmut Ettl, co-head of Austria's Financial Market Authority (FMA), said publicly that Austrian banks will use GOA state equity injections to shore up their CESEE subsidiaries and said the banks need help to prepare for more exchange-rate instability and a likely sharp increase in losses from emerging Europe. NOTE: Austrian banks have applied for a total of EUR 8 billion in state equity -- which should be disbursed by early February -- but so far only EUR 900 million has been disbursed to one bank (troubled but relatively small Hypo Alpe Adria (ref A). END NOTE. Austria's FMA has called on CESEE governments to assist banks active in their countries, regardless of ownership.

#### Nine Prominent European Banks Seek Rescue Plan

17. The GoA initiative reflects strong lobbying by Austrian banks engaged in CESEE and a January 23 meeting of the Austrian Finance Ministry (MoF) with representatives from the Austrian National Bank (OeNB), FMA, EBRD and IMF to discuss financial support for ailing CESEE economies and prevent a credit crunch, and rescue measures for banks engaged in CESEE.

18. Herbert Stepic, CEO of Raiffeisen International (RI) Bank, one of the biggest players in CESEE/CIS, is spearheading a group of nine major banks active in CESEE who are seeking a "masterplan" by the EU, ECB and local governments to assist banks active in the region. The nine banks are  
-- two Austrian banks: RI and Erste Bank  
-- two Italian banks: UniCredit (including its Austrian subsidiary Bank Austria) and Intesa Sanpaolo  
-- Belgian KBC

-- French Societe Generale  
-- German Bayern LB (owner of troubled Hypo Alpe  
Adria)  
-- Greek EFG and  
-- Swedish Swedbank.  
The banks characterize such a masterplan as a  
precautionary measure in case the situation  
deteriorates.

¶9. Stepic said economic difficulties in CESEE will  
soon hit the banking sector in those countries.  
Situations vary, but throughout the region the high  
dependency on foreign-currency loans is a problem.  
Therefore, banks active in CESEE have a strong need  
for fresh equity, which requires action by the EU and  
the national governments, according to Stepic. Erich  
Hampel, CEO of Bank Austria (which handles CESEE  
business for its parent UniCredit) said that 2009 and  
2010 will be very difficult years but that BA (like  
other Austrian banks) has no plans to retreat from  
those markets.

COMMENT  
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¶10. Austrian bankers and officials have changed their  
storyline over the past two weeks. Through the end of  
2008, CESEE markets were painted as a kind of refuge  
and blessing for Austrian banks (who had relatively  
little exposure to New York/London-centric CDO and  
CDS-type assets). Now Austrians see the region as a  
source of potentially acute risks, and the current  
initiative has an air of urgency. The Austrian  
banking sector is well capitalized and can draw on a  
huge asset/savings base (total balance sheet assets  
are over 1 trillion euros) to cover any losses -- but  
bankers would clearly prefer to avert a downward  
spiral in CESEE if the EU and IMF can mobilize in  
time. Importantly, banks like Raiffeisen do not want  
a line drawn at the EU's borders, one which would  
leave them highly exposed in markets such as Ukraine.

¶11. While the Austrian body politic stands firmly

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behind its banks, the notion (floated by some bankers)  
of a government-owned vehicle to take over troubled  
CESEE assets has not met a lot of sympathy here. END  
COMMENT.

KILNER